Supreme Court, U.S.
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No.

IN THE
Supreme Court of the United States
OCTOBER TERM, 1995

CITY OF MORGAN CITY,
Petitioner,

v.

SOUTH LOUISIANA ELECTRIC COOPERATIVE ASSOCIATION, CAJUN ELECTRIC POWER COOPERATIVE, INC., and THE UNITED STATES OF AMERICA, through the RURAL UTILITIES SERVICE,
Respondents.

Petition for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

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PETITION FOR A WRIT OF CERTIORARI

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11 See

QUESTIONS PRESENTED

1. Is a municipality barred by the doctrine of "frustration of federal purpose" from exercising its power of eminent domain to condemn the property of a utility that has received federal loans under the Rural Electrification Act, 7 U.S.C. §§ 901, *et seq.*?

2. Does Section 7 of the Rural Electrification Act, 7 U.S.C. § 907, require the approval of the Act's Administrator before a local government may exercise its power of eminent domain to take property belonging to a utility that has received an REAct loan?

PARTIES TO THE PROCEEDING BELOW

All parties to the proceeding below are named in the caption. The United States appeared below through the Rural Electrification Administration, an agency within the United States Department of Agriculture charged through its Administrator with responsibility for the Rural Electrification Act. As part of its reorganization of the Department of Agriculture, Congress has created a new federal agency within the Department, the Rural Utilities Service, and assigned to its Administrator the administration of the Rural Electrification Act. The caption of this Petition reflects that change.

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PETITION FOR A WRIT OF CERTIORARI

Petitioner City of Morgan City respectfully prays that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Fifth Circuit dated September 12, 1994, as supplemented by an opinion on rehearing dated April 3, 1995.

OPINIONS BELOW

The opinion of the United States Court of Appeals for the Fifth Circuit dated September 12, 1994, is reported at 31 F.3d 319, and is set forth in the Appendix at 1a. The April 3, 1995 decision on rehearing is reported at 49 F.3d 1074 and is set forth at App. 24a. The opinion of Judges Jones, Smith, and DeMoss, dissenting from denial of rehearing en banc, is reported at 49 F.3d at

1076, and is set forth at App. 28a. The opinion of the United States District Court for the Western District of Louisiana is reported at 837 F. Supp. 194 and is set forth at App. 12a. A decision of the Rural Electrification Administration relied upon by the district court and cited by the Court of Appeals is set forth at App. 35a.

JURISDICTIONAL STATEMENT

The judgment of the Court of Appeals was entered on September 12, 1994. The petition for rehearing was denied on April 3, 1995. This Court's jurisdiction rests on 28 U.S.C. § 1254(1).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

Relevant provisions of the Rural Electrification Act, 7 U.S.C. §§ 901 *et seq.*, are set forth at App. 76a, including 7 U.S.C. § 907, which is set forth at App. 76a-77a. The text of the Supremacy Clause, United States Constitution, art. VI, cl. 2, is set forth at App. 82a.

STATEMENT

Relying on "frustration of federal purpose," the court below held that by virtue of having obtained a federal loan under the Rural Electrification Act ("REAct") a utility providing service to customers within a municipality is immune from the municipality's exercise of its power of eminent domain. This "breathtaking federal power-grab" (49 F.3d at 1076; App. 28a) curtails the natural expansion of many cities that provide public power to their citizens and nullifies state laws and policies that afford municipalities the exclusive right to provide electric service to their citizens. The expansive vision of "frustration" on which the decision rests is in direct conflict with decisions of the state courts dealing with precisely this issue, is inconsistent with this Court's restrained approach to claims of implied preemption in areas of traditional state authority, and takes the "frustration" doctrine far from its constitutional roots.

Overview

It is the historic province of the states to regulate utilities and determine the areas in which utilities may operate within the state. Exercising that traditional power, most states afford municipalities in the state the right to be the exclusive providers of electric power to their citizens. In aid of that exclusive right, municipalities are granted the power of eminent domain; specifically, the power to take, upon payment of just compensation, the franchise and property of other utilities that previously operated within the municipality's boundaries. Consistent with these state policies, more than 2,000 towns and cities now provide electric power to their citizens. At any given time, many additional towns and cities are considering doing so.

As towns and cities develop, and the surrounding area becomes more densely populated (*i.e.*, less rural), the town or city will expectably seek to expand into adjacent suburban areas that are part of the larger urban community. Following annexation, towns and cities that provide electric service will exercise their right under state law to provide electricity to the citizens of the newly annexed areas. Along with other considerations addressed by elected officials in determining whether annexation is in the community's best interest, the opportunity to provide utility service to the new area is often an important economic factor in the decision to annex.

Revenue from the sale of municipal power often helps to finance other municipal services—such as street lights, sewers, and police and fire protection for existing areas or newly annexed areas. The lower price of municipal power often provides a correspondingly important reason why the citizens of adjacent areas seek to be annexed.[1]

[1] In addition, many municipalities are presently considering initiating municipal electric service because (1) they can provide their citizens lower price electric service through municipal power,

In addition, following annexation, those citizens will receive additional municipal benefits, often underwritten in part by municipal power. On the other hand, the current providers of electric service to the areas surrounding the urban center have a natural tendency to resist encroachment on their customer base.

Electric service to these surrounding areas is often provided by "rural electric cooperatives." [2] These cooperatives are typically beneficiaries of federal loans made available under the REAct—a federal program of low cost loans designed to encourage rural electrification. 31 F.3d at 322; App. 6a. Although the areas in question are no longer "rural," the rural utilities prize their service to those areas for that very reason. Their higher population density makes them more profitable to serve.[3] 31 F.3d at 324; App. 10a. In effect, REA borrowers use urban customers to subsidize rural customers, making it easier to repay loans or increase profits.

The clash of interests described above recurs frequently, for municipal annexation and expropriation are

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and (2) significant municipal revenue can be generated by the sale of electricity.

[2] Such cooperatives serve over 70% of the geographical land mass of this country. National Rural Electric Cooperative Association, *Management Issues Facing Rural Electric Systems: Recent Developments and Implications* 1 (1993).

[3] As the National Rural Electric Cooperative Association described the cooperative's economic interests in an *amicus* brief filed in support of the United States in the court below:

> [A]ttractive loads . . . are often in the higher density areas close to municipalities. Because of the profitability of serving areas, they become targets of municipal annexation and condemnation. Loss to municipalities of the right to service these territories makes it impossible for rural electric systems to realize the economics of scale and lower per-user costs that accompany service to higher density areas . . . .

Brief of Amicus Curiae National Rural Electric Cooperative Association in Support of the United States of America (October 5, 1993) at 12.

the product of natural demographic changes as people seek to avail themselves of the benefits of living near or within an urban center. A survey by the National Rural Electric Cooperative Association, reported to the court below, showed that at least 86 of its member cooperatives lost customers through municipal condemnations (resulting in the payment of approximately $80 million in compensation) in the period 1985-89.[4]

The decision of the court of appeals effectively barring municipal expropriation of the property of REA borrowers hems in many of the more than one hundred municipalities within the Fifth Circuit providing municipal power, affecting their annexation plans and their budgets. A similar bar applies in the Ninth Circuit.

The Parties To This Action

Petitioner City of Morgan City is a Louisiana municipality that has long provided electricity to its citizens. It has a total population of 17,000 and its utility serves about 6,000 customers. In January 1985, Morgan City annexed a small adjacent suburban area. In addition to affording the residents of the annexed area the right to take advantage of city services and participate in its political processes, Morgan City wishes to provide those citizens with the same low cost electric service that it affords its other citizens.

Respondent South Louisiana Electric Cooperative Association ("SLECA") is an electric cooperative that has received long-term, low-interest loans from the REA, secured by a general lien on SLECA's property and

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[4] *See* Final Report of the Territorial Integrity Committee, National Rural Electric Cooperative Association, November 1990, Appendix A, Annual Annexation Losses for RECS Responding to Annexation Survey (attached to the *amicus* brief of the NRECA in the court below). It appears that all of those condemnations would be barred by the rule established by the court below.

income.[5] Approximately 252 of SLECA's 14,828 customers are located in the area annexed by Morgan City.

On August 3, 1990, Morgan City brought this action pursuant to L.R.S. §§ 19:101 *et seq.* in Louisiana state court to expropriate certain SLECA property—including the exclusive right to serve the utility customers within the annexed area. On January 11, 1991, Respondent Cajun Electric Power Cooperative, Inc. ("Cajun"), a rural electric generation and transmission cooperative that provides power to SLECA, intervened.[6] Because of its security interest in SLECA's property, Respondent United States (through the REA) was joined as a third party defendant under 28 U.S.C. § 2410(a)(4). Section 2410 provides that the interests of a federal lienholder may be terminated according to the state law standards that govern the termination of a private lienholder's interests. Pursuant to 28 U.S.C. § 1444, the United States removed the case to the United States District Court for the Western District of Louisiana.

The Rural Electrification Act

The Rural Electrification Act ("REAct"), 7 U.S.C. §§ 901 *et seq.*, establishes a loan and guarantee program to assist electric utilities in financing service to rural areas. "Rural areas" are areas "*not* included within the boundaries of any urban area." *Id.* at § 913 (App. 80a). During the relevant time frame, the loan program was administered by the REA; pursuant to a recent internal reorganization of the Department of Agriculture, it is now administered by the Rural Utility Service. 7 U.S.C. § 6942.

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[5] SLECA owes approximately $25 million to the REA. 31 F.3d at 321 n.1; App. 2a.

[6] Cajun has received substantial REAct loans. Cajun provides power, through distribution cooperatives like SLECA, to approximately 337,000 customers. App. 41a. The 252 SLECA customers located in Morgan City are less than one tenth of one percent of the total population indirectly served by Cajun.

The REAct grants the agency no regulatory authority. *See Arkansas Elec. Coop. Corp. v. Arkansas Pub. Serv. Comm'n,* 461 U.S. 375, 385-89 (1983). The REAct provides the Administrator with authority over its borrowers, which borrow on the terms and conditions established by the REAct and the Administrator. The Administrator's powers are like those of a banker, deciding whether to extend credit and control ongoing relations with borrowers. *See* 7 U.S.C. §§ 902, 912, 912a (App. 76a-80a).

Administrative Action Relied Upon By The District Court

Relying on 7 U.S.C. § 907 (App. 76a), which prohibits borrowers from disposing of loan security, the REA has taken the position that it has the statutory power to veto a municipality's condemnation of the property of an REA borrower. SLECA asked the REA to exercise this claimed power to allow it to "retain the consumers Morgan City proposes to expropriate." App. 48a. In support of that effort, Cajun and SLECA made submissions to the REA staff. Morgan City—whose action was at issue—had not borrowed REA funds; it was, therefore, not subject to the REA's authority and was not involved in the administrative process purporting to pass on its action.

After hearing from Cajun and SLECA, REA *dis*approved Morgan City's expropriation of SLECA's property, noting, *inter alia,* that "the Morgan City expropriation should not be considered an isolated taking [because] if successful, it could mark the beginning of several actions by Morgan City and other municipalities to acquire property and territorial service right[s] of SLECA and other REA borrowers in Louisiana." App. 74a.

The District Court Decision

On the basis of this administrative determination, Respondents moved for summary judgment. They argued that because Section 907 required prior REA approval,

and approval was denied, the expropriation could not go forward. Under this view, the only issue for the court was whether the decision to deny approval was arbitrary or capricious. Morgan City opposed the motion, arguing, *inter alia*, that § 907 simply did not grant REA the authority to approve or disapprove its expropriation.

The district court granted Respondents' motion, holding that the agency record adequately supported REA's action. 837 F. Supp. at 199-200; App. 20a-21a. It declined to consider evidence tendered by Morgan City.[7]

The Court Of Appeals Decisions

The Fifth Circuit panel did not address the district court's ground for decision, leaving the statutory question —whether Section 907 provides the REA with authority to disapprove a municipal condemnation of a borrower's property—"for another day." The panel adopted instead the broader constitutional ground that the state-law expropriation is preempted because it "would frustrate a federal purpose." 31 F.3d at 322; App. 5a.[8]

The Fifth Circuit panel largely adopted the reasoning of the Ninth Circuit in *Public Utility Dist. No. 1 of Pend*

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[7] Morgan City tendered evidence to show that in light of the compensation that would be paid, and the schedule of future condemnations, the effect on SLECA was minor. Viewing the matter as involving review of the agency record, the district court rejected the evidentiary submission. On the same reasoning—and notwithstanding that Morgan City had not participated in the agency proceeding—the district court declined to allow Morgan City to conduct discovery. 837 F. Supp. at 195; App. 14a. In addition, the district court rejected Morgan City's contentions that because no approval authority was conferred by the REAct or by regulation, the agency decision was not "agency action" under 5 U.S.C. § 702, and, in any event, the applicable standard of review was that provided by 5 U.S.C. § 706(2)(B) rather than the "arbitrary and capricious" standard of 5 U.S.C. § 706(2)(A).

[8] The broader constitutional issue upon which the panel based its decision had *not* been raised in the district court. Following oral argument, the panel requested letter briefs on the "frustration" theory suggested by the Ninth Circuit cases.

Oreille County v. United States, 417 F.2d 200, 201-02 (9th Cir. 1969), holding that "[t]he condemnation of a portion of a federally subsidized rural electrification system, even if compensated for under state law, would impair Congress's objective of providing reliable, low-cost electricity to rural America." 31 F.3d at 323; App. 8a.[9] The panel noted that this expropriation "would pave the way for piecemeal erosion of other high-density service areas adjacent to Morgan City and other cities." Thus, the proposed expropriation would " 'stand as an obstacle' to the repayment of federal loans, to the financial viability of federally financed electricity cooperatives, and ultimately to the maintenance of electricity service to rural areas." *Id.* at 324; App. 10a.[10]

In denying rehearing, the panel addressed *Arkansas Electric*, 461 U.S. 375, which it had failed to mention in its earlier opinion. On rehearing, the panel discerned a "general federal policy of protecting the integrity of the REA's security interests." 49 F.3d at 1075; App. 26a. The panel again emphasized the likelihood of future expansion activities by Morgan City and other cities. It also made reference to REA "findings," noting the lost revenue and operating margins that would result from the proposed expropriation.

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[9] The panel also cited an earlier Fifth Circuit decision, *City of Madison v. Bear Creek Water Ass'n, Inc.*, 816 F.2d 1057 (5th Cir. 1987), which addressed a statute that *expressly* prohibited annexation of a water association's territory. 7 U.S.C. § 1926(b).

[10] As noted above, Respondents had not made an independent evidentiary submission in the district court of the kind that would support a *de novo* judicial ruling on "frustration." Rather, the REA proceeded as if this was an action to review an agency's exercise of its statutory power, presenting the administrative decision for APA review. *See* 837 F. Supp. at 199; App. 21a. In reaching the constitutional issue, the panel nonetheless adverted generally to administrative findings arising from the essentially "friendly" agency proceeding in which Cajun and SLECA had submitted materials to the agency, but Morgan City did not participate.

Dissenting from denial of rehearing *en banc*, Circuit Judge Edith H. Jones, writing for herself and Judges Jerry E. Smith and DeMoss, described the panel decision as having approved "a breathtaking federal power-grab by REA from local government units that otherwise enjoy broad eminent domain authority." 49 F.3d at 1076; App. 28a. The dissenters noted that neither the REAct itself nor the agency's regulations contemplate preemption of this "quintessential local power"; in fact, by requiring the REA to consider the risks "of loss of borrower's service territory from annexation" in assessing the feasibility of the loan, the REA's own regulations assumed that such annexations are *not* preempted.

The dissenting judges viewed the panel's decision as inconsistent with *Arkansas Electric*, 461 U.S. 375, which rejected an REA claim that state regulation of an REA borrower's rates would "frustrate" federal objectives. Noting that state rate regulation has far greater potential to hobble an REA borrower than does eminent domain, the dissenters found *Arkansas Electric* controlling. *Id.* at 1076-77; App. 28a.

The dissenters noted that § 907 (upon which the district court rested) merely "permits REA, like any lender, to prevent voluntary alienation of its collateral by the borrower; it says nothing about REA's ability to forestall *involuntary* condemnation of service territory." 49 F.3d at 1077; App. 31a (emphasis in original). The dissenting judges emphasized the breadth of the panel's decision, based on factual assumptions drawn from the REA record, without benefit of "hearing or trial," noting that if this condemnation, involving 252 customers, frustrates the REAct, it would be hard to imagine "what exercise of eminent domain would not do so." *Id.* at 1078; App. 32a.

Finally, the dissent commented on the "high degree of judicial policymaking" associated with the "frustration doctrine," *id.* at 1079; App. 34a (quoting *The Law of*

Preemption, a Report of the Appellate Judges Conference, American Bar Association 38 (1991) (authored by Judges Higginbotham, Seymour, Sneed, Starr, Clark, and Criswell)), and summarized the doctrine as "highly problematic, rarely utilized by the Supreme Court and of dubious propriety."

REASONS FOR ISSUING THE WRIT

I. THE DECISION OF THE COURT BELOW FRUSTRATES STATE POLICY, CONFLICTS WITH STATE COURT DECISIONS, AND IMPEDES THE GROWTH OF MUNICIPALITIES PROVIDING PUBLIC POWER TO THEIR CITIZENS

The court of appeals' decision bars municipalities from exercising the power, upon the payment of just compensation, to expropriate the property of utilities operating within their boundaries. The basis for this preemption is the utilities' receipt of, and continuing obligation under, federal loans.

The court of appeals proceeded on the economic understanding that the customers in the annexed area at issue—now citizens of Morgan City—were profitable to serve because they no longer lived in a rural area. If Morgan City exercised its state law prerogative to provide these citizens with municipal electric service, SLECA would lose an urban source of revenue, potentially affecting charges to its rural customers or making it more difficult for SLECA to repay its loans. The panel ignored the fact that SLECA would be compensated for the taking of its franchise based in part on the value of the lost revenue.

Apart from the broader precedential implications of finding receipt of federal loan money to be a source of immunity from state law,[11] the panel's decision has an immediate and lasting impact on cities providing munici-

[11] That rationale could create immunity from any number of state laws that make it harder for an REA borrower to repay its loans, *e.g.*, tax, environmental, or labor laws.

pal power within the Fifth Circuit—a circuit that includes many of the 2,000 municipalities in the Nation providing public power to their citizens. The impact of the decision falls not only on the scope of electric service provided by municipalities but also upon basic municipal planning and expansion decisions. In exchange for providing water, sewer, public lighting, or even police and fire service to a group of new citizens, a municipality may count on revenue generated by providing electric power to a newly annexed area.

The situation presented here recurs frequently,[12] as cities providing public power expand into contiguous areas served by cooperatives, or consider initiating municipal electric service to their citizens. In order to provide such service, municipalities must exercise their power of eminent domain. It is entirely reasonable for the state to afford municipalities the power to exercise eminent domain power in these circumstances. It is equally reasonable for the state to choose a public policy under which citizens who receive valuable municipal benefits are asked to share the burden of generating revenue for the city through the purchase of electric power from the municipal utility.

To be sure, the Ninth Circuit decisions cited by the court below had established a substantial barrier to expropriation of cooperative territory in that Circuit.[13] While ill-conceived, the Ninth Circuit's rule was of somewhat limited *practical* effect, in part because there are few municipal utilities within that Circuit abutting areas

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[12] *See* text at n.1 *supra*. Indeed, the agency referred to the likelihood of future annexations by other municipalities. App. 63a; 74a.

[13] *Public Utility Dist. No. 1 of Franklin County v. Big Bend Elec. Coop., Inc.*, 618 F.2d 601 (9th Cir. 1980), and *Pend Oreille, supra*, 417 F.2d 200.

served by REAct borrowers.[14] The Fifth Circuit's ruling represents a far greater intrusion, affecting many municipalities.

The decision effectively creates a constitutional barrier to municipal expropriation of cooperative property. It states a general rule of preemption, not some narrow fact-bound exception. As the dissenters pointed out below, if preemption was warranted on these facts, involving an expropriation of 252 customers, it is difficult to conceive a permissible expropriation. 49 F.3d at 1078; App. 32a. Nothing in the panel decision reflected close attention to the facts of the particular expropriation. The panel's language (and its two quotations from the Ninth Circuit's *Pend Oreille* decision) took the form of broad statements to the effect that the taking of the cooperative's profitable customers presented a facial affront to federal objectives. 31 F.3d at 323; App. 9a-10a. The panel's only discussion of the facts was in rejecting the argument that the expropriation of 252 customers was *de minimis*. This was rejected based on the generality that even a small taking "could well leave federally funded cooperatives financially unable to continue service to the remaining low-density areas . . . ." 31 F.3d at 324; App. 10a.

Neither is the breadth of the panel's opinion obscured by the references on rehearing to gross revenues and system operating margins in the annexed territory. It is in the very nature of the demographic situation presented by municipal expropriation that the customers at issue provide "high operating margins" to a rural cooperative because they are in a densely populated area, whereas

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[14] The condemnations at issue in the Ninth Circuit cases were by public utility districts, which have fixed, permanent boundaries. The actions of the public utility district might therefore have been characterized as selecting those customers within its boundaries that were most profitable to serve. The Ninth Circuit cases did not squarely address the natural demographic processes that give rise to municipal annexation and expropriation.

the remainder of its customers are presumably in rural (*i.e.*, low density, low operating margin) areas.[15] Thus, such takings will always involve the loss of the cooperative's most profitable customers. Even if it could be argued that there are cases involving takings more *de minimis* than this one, and that some cases will turn on particular facts, the mere possibility that a federal court might ultimately decide to approve the expropriation does not provide the assurance that a city needs in deciding whether to go forward with a possible annexation.

Indeed, the breadth of the Fifth Circuit's decision is reflected in a recent Oklahoma district court case following its reasoning. *See City of Stilwell v. Ozarks Rural Elec. Coop. Corp.*, 870 F. Supp. 1025, 1030 (E.D. Okla. 1994) (condemnation of 154 customers of an REA borrower "frustrate[d] the federal purpose," even though the REA did not "disapprove" it). Thus, this case is of lasting importance to cities within and without the Fifth (and Ninth) Circuits, whether they are providing municipal power now, or merely considering doing so.

The state courts have squarely rejected the REA's "frustration" theory. The Supreme Court of Indiana held that a municipality's condemnation of an REA borrower's service territory in an annexed area did not frustrate the REAct's purpose. *Decatur County Rural Elec. Membership Corp. v. Public Serv. Co.*, 261 Ind. 128, 301 N.E.2d 191, 198 (1973). The court was "unable to discern any clash between the State of Indiana and the United States" because "the purpose for [a rural cooperative's] existence expires when the area which it serves becomes 'urbanized.' " 301 N.E.2d at 198. Similarly, the Minnesota Court of

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[15] Moreover, the panel's general references to REA "findings" only compounds the problem. 49 F.3d at 1076; App. 27a. If based on facts at all, the court of appeals' ruling was based on constitutional fact-finding, which was for the federal court to find based on the evidence before it. It is up to the agency, seeking to hold the state action unconstitutional, to prove its case. In this constitutional setting, the agency's position is addressed *de novo*; it is not subject to the deferential "arbitrary and capricious" standard.

Appeals, in rejecting the REA's "frustration" argument, expressly declined to follow the reasoning of the Ninth Circuit cases and the decision of the district court in this case, finding "more persuasive the views stated by the Supreme Court in *Arkansas Elec. Coop. . . .*" *City of Rochester v. Peoples Co-op Power Ass'n, Inc.*, 505 N.W.2d 621, 625-26 (Minn. App. 1993). The conflict between the state courts and the federal circuits on this issue is manifest.

II. THE DECISION OF THE COURT OF APPEALS IS INCONSISTENT WITH THIS COURT'S PREEMPTION DECISIONS

1. It is one thing to say (as the Supremacy Clause, art. VI, cl. 2, makes clear) that federal *law* trumps state law. It is far more problematic to say that federal courts are empowered to identify abstract federal "objectives" and then employ those federal objectives to override state law. Unless *Congress* has decided the issue presented, whether directly or by fair implication, a federal court oversteps both its judicial role and the limits of federal power when it nullifies state law armed only with its assumptions about the scope of federal "objectives."

Defining the *limits* of a federal program is just as much a policy choice committed to Congress as is conceiving the program in the first instance. "[T]he purpose of a statute includes not only what it sets out to change, *but also what it resolves to leave alone*. The best evidence of that purpose is the statutory text . . . ." *West Virginia Univ. Hosps., Inc. v. Casey*, 499 U.S. 83, 98-99 (1991) (emphasis added).[16] Thus, to hold that a federal objective overrides state policies supporting the right of

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[16] "Deciding what competing values will or will not be sacrificed to the achievement of a particular objective is the very essence of legislative choice—and it frustrates rather than effectuates legislative intent simplistically to assume that *whatever* furthers the statute's primary objective must be the law." *Rodriguez v. United States*, 480 U.S. 522, 526 (1987) (emphasis in original).

municipalities to expropriate property in order to provide electricity to their residents, is itself to make an important policy choice.

This Court's cases establish a *constitutional* presumption that Congress intended to leave traditional exercises of state and local authority undisturbed. *See infra* at 17-18. To assume, as did the court below, that Congress would have chosen to override state and local authority to further the general objective of a federal program turns that constitutional presumption on its head.

Building on the Ninth Circuit cases, the Fifth Circuit gave a literal reading to the language from *Hines v. Davidowitz*, 312 U.S. 52, 67 (1941), that state law standing "as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress" is preempted. It applied that language as if it were an invitation to the federal courts to nullify local law impeding the *general* goals of federal programs. In so doing, the court extended the "frustration doctrine" far beyond its constitutional premises. It cannot be enough under the Constitution that state law impedes some general federal goal. *See Exxon Corp. v. Governor of Maryland*, 437 U.S. 117, 133-34 (1978). There must be evidence that Congress actually made—either expressly, or at least impliedly—the specific policy judgment that the court seeks to enforce.[17]

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[17] *See generally Commonwealth Edison Co. v. Montana*, 453 U.S. 609, 634 (1981) ("'[P]re-emption of state law by federal statute or regulation is not favored in the absence of persuasive reasons—either that the nature of the regulated subject matter permits no other conclusion, or that the Congress has unmistakably so ordained'"); *CTS Corp. v. Dynamics Corp. of Am.*, 481 U.S. 69, 79, 86 (1987) (finding no preemption based on the frustration doctrine where a state law was "consistent with the text and purposes of" the federal law at issue); *English v. General Elec. Co.*, 496 U.S. 72, 79 (1990). *See also BFP v. Resolution Trust Corp.*, 114 S. Ct. 1757, 1764 (1994) ("Federal statutes impinging upon important state interests 'cannot . . . be construed without regard to the implications of our dual system of government'"); *id.* at

In fact, in a related context, this Court cautioned against the very error that the panel made here: mistaking a federal program's overall goal for an intention to achieve that goal "at all costs." *Pacific Gas & Elec. Co. v. State Energy Resources Conservation & Dev. Comm'n*, 461 U.S. 190, 222 (1983). In *Pacific Gas*, the purpose of the statute in question "was . . . the promotion of nuclear power." *Id.* at 221. The Court nonetheless rejected the argument that state law impeding that objective frustrated the "full purposes and objectives of Congress":

> The Court of Appeals is right, however, that the promotion of nuclear power is not to be accomplished "at all costs." . . . [T]he legal reality remains that Congress has left sufficient authority to the States to allow the development of nuclear power to be slowed or even stopped for economic reasons. Given this statutory scheme, it is for Congress to rethink the division of regulatory authority in light of its possible exercise by the States to undercut a federal objective. The courts should not assume the role which our system assigns to Congress.

Id. at 222-23 (emphasis added). Here too, Congress left in place traditional state authority over utilities, including REA borrowers.

2. The court of appeals panel literally ignored this Court's repeated admonitions that any preemption inquiry must begin with the "assumption that Congress did not intend to displace state law." *Maryland v. Louisiana*, 451 U.S. 725, 746 (1981). This "strong presumption against pre-emption" (*Cipollone v. Liggett Group, Inc.*, 505 U.S. ——, 112 S. Ct. 2608, 2621 (1992)) avoids "unintended encroachment on the authority of the States." *CSX Transp., Inc. v. Easterwood*, 113 S. Ct. 1732, 1737 (1993). The rule against preemption is strongest where

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1765-66 ("where the intent to override is doubtful, our federal system demands deference to long established traditions of state regulation").

the matter involves "a field which the States have traditionally occupied." *Rice v. Santa Fe Elevator Corp.*, 331 U.S. 218, 230 (1947). "Indeed, in cases like this one, where federal law is said to bar state action in fields of traditional state regulation [the Court has] worked on the 'assumption that the historic police powers of the States were not to be superseded . . . unless that was the clear and manifest purpose of Congress.' " *New York Conf. of Blue Cross & Blue Shield Plans v. Travelers Ins. Co.*, 63 U.S.L.W. 4372, 4374 (April 26, 1995) (citations omitted). The decision of the Fifth Circuit panel fails even to pay lip service to that presumption and the principles on which it is based.

Utility regulation is "one of the most important of the functions traditionally associated with the police power of the States." *Arkansas Electric*, 461 U.S. at 377. Because it is a " 'field which the states have traditionally occupied . . . we start with the assumption that the historic police powers of the states were not to be superseded . . . unless that was the clear and manifest purpose of Congress.' " *Pacific Gas & Elec. Co.*, 461 U.S. at 206 (citation omitted).

The expropriation at issue in this case, however, involves matters even more fundamental than utility regulation. With respect to the same Louisiana statute authorizing the expropriation here, this Court remarked on the "special nature of eminent domain" and its intimate connection "with sovereign prerogative." *Louisiana Power & Light Co. v. City of Thibodaux*, 360 U.S. 25, 28-29 (1959). Equally fundamental to sovereignty is the power of a local government to define its political boundaries. There is no indication that Congress sought to interfere with the core political decisions associated with annexation, or the traditional assumption that a municipality with state approval may expropriate property in order to provide economical electric service to its citizens. Finally, nothing in the REAct suggests that Congress regarded the "just compensation" given other citizens

when their property is taken to be insufficient for REA borrowers.

Absent evidence that *Congress* has effectively made the policy choice at issue, a federal court should have *no* authority to impose its own notion of federal policy under the guise of a constitutional rule.

3. Congress could have given REA borrowers immunity from state laws impairing their ability to repay their loans, or allowed the agency to do so. Congress could have given the REA the power to assign service areas to borrowers; instead it left this area of traditional state authority untouched. Congress also could have *expressly* limited the power of municipalities to annex territory of an REA borrower, as it has done under *other* lending programs. *E.g.*, 7 U.S.C. § 1926(b) (water association's service area "shall not be curtailed or limited by the inclusion of the area served by such association within the boundaries of any municipal corporation"). But Congress did none of this expressly, and the court below suggested no reason to believe that Congress sought implicitly to displace the historic prerogative of cities to provide electric service to their citizens or otherwise interfere with state control over utility service areas. These are areas that Congress "left alone." *West Virginia Univ. Hosps.*, 499 U.S. at 98.

4. The panel below offered no reason to believe that the federal purposes that it found preemptive were *actually* congressional purposes. For example, it cited no evidence that Congress wanted urban power customers to subsidize rural customers. Congress encouraged rural electrification through favorable loans, *not* a subsidy achieved by granting borrowers a protected service territory.

Though the court below cited an apparent federal interest in repayment of federal loans, "[t]o the extent the REA believes that states must adopt rules of law that always allow federal lenders to recoup their investments,

it is mistaken." *Wabash Valley Power Ass'n, Inc. v. REA*, 903 F.2d 445, 454 (7th Cir. 1990). When a federal agency acts as lender, its loans are subject to state law and the same risks that affect the repayment of private loans. Applying state law to federal loans, therefore, does "*not* frustrate the objectives of the lending programs." *United States v. Kimbell Foods, Inc.*, 440 U.S. 715, 734 (1979).

Because loans are made "on the assumption that state regulation would apply" (*Wabash*, 903 F.2d at 455), a federal lender should consider the possibility of adverse state action *before* making a loan. *See Kimbell Foods*, 440 U.S. at 736-37. The ability to take the possibility of annexation into account in deciding *whether* to make a loan belies the claim of irreconcilable conflict between state law and the federal loan program. *See Northwest Centr. Pipeline Corp. v. State Corp. Comm'n of Kansas*, 489 U.S. 403, 517 (1989) (agency "will recognize [state regulation] as part of the environment in which appellant conducts its business, and will make its own decisions with that in mind"). A federal loan program would therefore seem to be a most unlikely source of preemption.

In fact, by regulation, the REA must specifically consider the risks posed by municipal annexation of a borrower's service area in determining whether the loan is feasible. 7 C.F.R. § 1710.112(b)(5).[18] As the dissenting judges emphasized below, having guessed wrong, or made

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[18] The regulations provide:

> § 1710.112 Loan Feasibility
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> * * *
>
> (b) . . . RUS will use the following criteria to evaluate loan feasibility:
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> * * *
>
> (5) Risks of loss of portions of the borrower's service territory from annexation or other causes will not substantially impair loan feasibility.

7 C.F.R. § 1710.112(b)(5) (1995) (emphasis added).

insufficient investigation of the facts, the agency cannot fairly enlist a federal court to exonerate it for the consequences of its faulty prediction. *See* 49 F.3d at 1078; App. 32a-33a.

5. The Ninth Circuit rule relied upon by the Fifth Circuit panel is wholly out of step with this Court's subsequent decisions in *Kimbell Foods* (as discussed above) and *Arkansas Electric*. As emphasized by the dissenters below, *Arkansas Electric* expressly rejected the argument that state regulation of an REA borrower's rates would frustrate the REAct's objectives. 461 U.S. at 385-86. The Court emphasized that the REA is a "lending agency rather than a classic public utility regulatory body." *Id.* at 386. The REAct thus reflects no intention to displace the traditional authority of the states over utilities. The Court then stated the rule that the Fifth Circuit panel disregarded: the "relevant inquiry . . . is not whether Congress authorized or expected such [state] regulation, *but whether it intended by its own actions to forbid it.*" *Id.* at 388 n.11 (emphasis added).

The panel below addressed *Arkansas Electric* only on rehearing. It noted that *Arkansas Electric* left open the possibility that state action might so seriously compromise the "ability of the [cooperative] to repay its loans, as to be implicitly preempted by the [REAct]." 49 F.3d at 1075; App. 25a (quoting *Arkansas Electric*, 461 U.S. at 389). This case presents the opportunity to cast light on that possibility—a possibility that is itself difficult to reconcile with *Kimbell Foods* or this Court's repeated admonitions that preemption ought not be found absent a manifest conflict or clear preemptive intent.

In any event, it is difficult to suggest that the panel in this case actually framed its ruling on the terms that *Arkansas Electric* left open.[19] The panel did not discuss

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[19] Moreover, the Ninth Circuit rule quoted by the panel contemplates preemption even though the compensation paid for the taking

the extent to which the ability to repay loans would be impaired—except in the general sense that a reduction of gross revenue makes it more difficult to repay one's loans. Moreover, it would seem that any effort to address that issue would have had to consider (at least) the compensation paid for the taking—including that portion of the compensation that would reflect lost future revenue.

6. The broad language often used by this Court to describe "frustration" plainly contributed to the error of the court below. Nonetheless, claims of "frustration" have almost always been *rejected* by this Court.[20] While the *Hines dictum* is frequently repeated, it is hard to find examples of "frustration" applied independent of other, better established grounds of preemption to support a decision.[21] "Frustration" is often used in connection with

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would allow the federal loan to be repaid. 31 F.3d at 323-24; App. 8a-9a.

[20] *E.g., Freightliner Corp. v. Myrick*, 63 U.S.L.W. 4265, 4266 (April 18, 1995) ("A finding of liability against petitioners would undermine no federal objectives or purposes . . ., since none exist"); *CTS Corp. v. Dynamics Corp. of Am.*, 481 U.S. 69, 79, 86 (1987); *Pacific Gas & Elec. Co. v. State Energy Resources Conservation & Dev. Comm'n*, 461 U.S. 190, 220-23 (1983); *Commonwealth Edison Co. v. Montana*, 453 U.S. 609, 636 (1981); *Exxon Corp. v. Governor of Maryland*, 437 U.S. 117, 133-34 (1978); *Brotherhood of Locomotive Engineers v. Chicago, Rock Island & Pacific Railroad Co.*, 382 U.S. 423, 429, 437 (1966).

[21] For example, *Michigan Canners & Freezers Ass'n, Inc. v. Agriculture Marketing and Bargaining Bd.*, 467 U.S. 461 (1984), involved an actual conflict between state law and express provisions and "theme" of the federal statute. *Id.* at 471. "[B]ecause the [state law] authorizes . . . conduct that the federal Act forbids, it 'stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress.'" *Id.* at 478.

International Paper Co. v. Ouellette, 479 U.S. 481 (1987), rested on the notion that the Clean Water Act required uniformity. *See also Gade v. National Solid Wastes Management Ass'n*, 505 U.S. ——, 112 S. Ct. 2374, 2383 (1992) (plurality), using "frustration" to enforce uniformity and as a short-hand for "conflict" (*id.* at

preemption of state law to enforce federal "uniformity," though it is sometimes used to describe actual conflict as well.

In *Hines* itself, the "frustration" language simply conflated two other, well established bases of preemption, "actual conflict" preemption, and occupation of the field. *See The Law of Preemption, a Report of the Appellate Judges Conference*, American Bar Association, at 27. "Frustration" had no independent significance; Congress occupied the field in an area of unique federal concern. *Id.*

Significantly, the only case of this Court cited by the Fifth Circuit panel to support its "frustration" finding, *Xerox Corp. v. County of Harris*, 459 U.S. 145 (1982), does not even mention "frustration." The narrow purposes of the federal statute at issue was to create duty-free enclaves. That purpose was historic, concrete, and arose out of federal control of foreign commerce. Like other "uniformity" cases, the statute's basic structure demonstrated Congress' purpose to bar all duties on the goods in question pending export, whether federal or state.

Applied as it was by the court of appeals panel, the "frustration" doctrine is "highly problematic," serving as a constitutional springboard for a "high degree of judicial policymaking" that displaces the legislative branch and the constitutional sovereignty of the states. 49 F.3d at 1078-79; App. 34a.

2386 n.2); *see id.* at 2389-90 (Kennedy, J., concurring) (defining conflict narrowly).

Felder v. Casey, 487 U.S. 136 (1988), used "frustration" but relied on the historic rule that a "federal right cannot be defeated by the forms of local practice." *Id.* at 138, 139-40, 150.

III. THE DECISION BELOW IS NOT SUSTAINABLE ON THE STATUTORY GROUND EMPLOYED BY THE DISTRICT COURT

Although the court of appeals reached out to rest on a broader constitutional theory, this case has its origins in the REA's assertion that 7 U.S.C. § 907 authorizes the REAct's Administrator to veto a municipal condemnation of a borrower's property. The court of appeals' refusal to adopt this primarily statutory ground for decision suggests, at a minimum, that the panel was not readily persuaded by its merit. The statutory theory was squarely rejected by the only appellate court that did address it.[22] It is without support in the REAct's language or structure. Section 907 provides that:

> *No borrower of funds* . . . shall, without approval of the Administrator, sell or dispose of its property, rights, or franchises . . . until any loan obtained from the Rural Electrification Administration . . . shall have been repaid.

7 U.S.C. § 907 (emphasis added). Consistent with the REAct's overall structure, this paragraph imposes an obligation upon a *"borrower of funds."* Like almost *any* borrower providing loan security, an REA borrower is barred from disposing of its loan security without its lender's consent. App. 76a-77a.

A condemnation, however, takes place by operation of law, irrespective of any action by, or even the wishes of, the property owner. The *condemnee* does not dispose of its property or participate in setting the compensation.[23] As explained in *City of Rochester*:

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[22] *See City of Rochester v. Peoples Co-op Power Ass'n, Inc.*, 505 N.W.2d 621, 625-26 (Minn. App. 1993).

[23] The legislative history reflects the fact that the provision was designed to prevent borrowers from voluntarily transferring the benefits of subsidized loans to private, for-profit companies. 80 Cong. Rec. 2168, 3304-06, 3317, 7248, 7362, 7675; Hearings on S. 34-83 Before the House Committee on Interstate and Foreign Commerce, 74th Cong., 2nd Sess. 74 (1936).

> The Act restricts actions by the "borrower of funds" —in this case, Peoples. Peoples itself is not selling or disposing of its property; rather, the City is taking that property from Peoples. Important concerns justify such a distinction. Voluntary sales or disposals of REA-financed property by a borrower would not guarantee fair or adequate compensation. Condemnation proceedings, on the other hand, entail a careful determination and payment of fair value for that property.

505 N.W.2d at 625.

Nothing in the REAct subjects any third party to REA authority. In fact, the *first* paragraph of § 907 addresses *in*voluntary dispositions—forced sales. For forced sales, the REA is *not* given veto power, but only a right of redemption. 7 U.S.C. § 907. Only with respect to the actions of its borrower—with whom it has a contract—does the REA have approval power.

CONCLUSION

The petition for writ of certiorari should be granted.

Respectfully submitted,

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